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INFO RUEHZL/EUROPEAN POLITICAL COLLECTIVE PRIORITY

C O N F I D E N T I A L SECTION 01 OF 02 STOCKHOLM 000570

SIPDIS

TREASURY FOR ERIC MEYER, DAVID WRIGHT
USEU FOR MATHEW HAARSAGER

E.O. 12958: DECL: 08/25/2019

TAGS: [ECON](#) [EFIN](#) [PGOV](#) [PREL](#) [SENV](#) [SW](#)

SUBJECT: SWEDEN,S PLANS FOR THE G-20, CONCERNS ABOUT THE
BALTIKS

Classified By: CLASSIFIED BY DCM ROBERT SILVERMAN, REASONS 1.5 (B) AND
(D)

¶1. (C) Summary: In a meeting with the U.S. Ambassador, Sweden,s Finance Minister Anders Borg praised the new mind set of the U.S. Administration that has us participating in international institutions. He urged the U.S. to keep countries focused on the political need to prevent an economic collapse in the Baltics, opining that the Baltics still faced a 50% chance of collapse by December. Such a decline would not threaten Sweden, he said, but would have consequences for the region. At the G20, Sweden hopes for a strong statement showing political will to finance measures against climate change. Borg described EU efforts to improve regulation of the financial system, expressing concern that the unavoidable result would be separate U.S. and European capital markets, which could prove problematic and protectionist. End summary

Welcoming U.S. Willingness to Work as a Partner

¶2. (C) On August 25, the Ambassador paid his introductory courtesy call on Finance Minister Anders Borg. Borg began by describing enthusiasm in Europe and especially among Sweden,s political elite for the new U.S. mind frame under the Obama Administration whereby the U.S. had become more participatory in international institutions. He praised the &extraordinary8 statements by Secretary Geitner that the U.S. would be part of in the IMF Financial Sector Assessment program (FSAP) and related processes. He said U.S. participation was key to the credibility of all such programs. The &big shift8 in the U.S. attitude that had us now being a partner in such efforts, he said, made it a lot easier to be a friend of the United States. He noted that even his children were sporting Obama T-shirts around the house.

U.S. Needs to Keep the Focus on the Baltics

¶3. (C) In response to the Ambassador,s question on what else the U.S. could be doing, Borg said it was important for the U.S. to keep the international focus on the Baltics, acting like an uncle to tell the world it is not just a simple matter of economics, but a political matter that some smaller countries in Eastern Europe are also important, including these &small, newly established democracies with a large neighbor who can be aggressive.8 Borg noted that U.S. Treasury is &very constructive8 and doing a &very, very good, very constructive job8 in this regard.

¶4. (C) Borg expressed the hope that we are seeing some kind of stabilization in Latvia. He said Latvia could be on one of two paths: The good path of the government pulling together, delivering on its promises to the European Commission and the IMF; political support for those commitments not declining; and global economic recovery. Or,

Latvia could be on the bad path of no political support for keeping its commitments, no delivery on those commitments, no global recovery, and a drop in oil prices that would bring problems for Russia, and be quite problematic for Russian behavior toward Latvia. He said politically we cannot have the Baltics becoming failing states, or something that Russia would dub a failing state to justify picking up cheap collateral through Russian investment geared to gaining dominance in these countries.

¶ 15. (C) Borg noted that substantial problems remained in all the Baltic economies. Twenty-five percent current deficits had gone to balance within six months, but large imbalances remained, such as the very weak export sector. On the other hand, he said, all three economies were quite flexible, had flexible labor laws and the &spirit8 where they believed they would be strong economically in the future. Although you can see positive signs, he cautioned, there remains a 50% probability that it could all break down by year-end.

Spillover Risk from A Baltic Collapse

¶ 16. (C) Borg said a Baltic collapse was a major risk for the region, but not for Sweden. Borg said it was crucial for Sweden that Latvia was saved from collapse in December 2008 and June 2009, but now Swedish companies were again getting credit on international markets making the economy less vulnerable. There would be problems in one or two specific banks, but one of them was owned by the Wallenberg family which had its own good cash balance. The problem, Borg said, is Swedbank, but a problem with one bank is not a banking crisis. (Comment: Swedbank is one of the four large banking

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groups in Sweden that combined handle 80% of banking activity in Sweden.)

G-20 Needs to Issue Strong Statement on Climate Change

¶ 17. (C) In response to the Ambassador,s question about Sweden,s goals for the G20 Summit, Borg noted that now that financial markets were &a bit more normal8 we should do two things: build on work already done to prevent a repeat economic crisis; and increase emphasis on financing efforts to combat climate change. In order to have success at Cop-15, Borg said, we need a strong G20 statement from U.S. and European leaders showing strong political will to find a solution on financing efforts against climate change.

Financial Regulatory Reform Yielding Separate U.S. and European Systems

¶ 18. (C) On financial reform, Borg explained that we no longer need acute crisis management, but to work on the Bretton Woods institutions. Noting that Sweden and the U.S. were co-chairs the Financing Group, he said U.S. Treasury was actually leading, which was okay because Treasury was pushing in the right direction toward solutions and increased efficiency.

¶ 19. (C) Borg said we need to strengthen many parts of the financial regulatory system, &We don,t need more or less regulation, we need better regulation8. He said the EU was working on a macrosupervisory Board, cooperation between Financial Supervisory Authorities, cooperation between national Central Banks, common European institutions, and new common decision making given the challenges of cross-border banking. He cited the need for strong regulation of the internal business of the banking system, for example bonuses and renumeration must consider society,s interests as well as the bank,s interests because taxpayers could be forced to pay the bill of a failed bank.

¶ 110. (C) Borg said the EU does not want to hinder capital markets, but private equity needs prudent regulation. He said that hedge funds and private equity funds had not been a

cause of the current crisis, but could be a problem in the long-run. He cited Long Term Capital Management (LTCM) as one hedge fund that did almost devastate the financial sector in the past. Noting the need for prudence in risk-taking, Borg said it was reasonable that firms should be held responsible for risk they are exposed to, what kind of balance sheets they main, their valuation, and similar matters.

¶11. (C) Borg said that in a perfect world, there would be only one set of regulations, and it would be better to have one institution. But, we live in an imperfect where the U.S. and Europe will each have one institution, which &could cause some problems.⁸ He said he was aware that having one capital market in Europe and one in the U.S. &could be protectionist and problematic.⁸

Sweden to Address Long-Term Problems in the Labor Market

¶12. (C) The DCM then asked Borg about the government's current negotiations over the government budget. Borg said his government would implement a second round of crisis measures this coming year. Because public finances had been better than expected, the deficit would decline to 1.3 or 1.4% by 2011 (after being 3.5% in 2009 and 3.4% in 2010). Measures taken include temporary measures to stimulate demand such as local government support, infrastructure, temporary education schemes and changes to labor laws. The next round of the government's response was dealing with long-term structural problems in the labor market. Borg explained that 300,000 jobs had been lost in the current crisis and 100,000 of those losses could be permanent. The government, he said, needed to go more to make work pay and incentivize people to stay in the labor market rather than the current cycle: unemployment benefits; job re-training; and then directly into early retirement. He noted that in his public statements, he was careful not to commit to specific job creation benefits from government measures, since you could not ensure delivery.

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